

**INDIANA STATE TEACHERS' RETIREMENT FUND**

**INDIANA STATE TEACHERS' RETIREMENT FUND  
RESTATEMENT OF INVESTMENT POLICY**

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## **I. INTRODUCTION**

### **II. Description of TRF**

The Indiana State Teachers' Retirement Fund ("TRF") was established in 1915, to pay retirement, disability, death, and survivor benefits to public school teachers and administrators, regularly employed teachers at certain state universities and other educational institutions, and certain other education employees. Pursuant to Indiana law and the Internal Revenue Code, TRF must be operated for the exclusive benefit of, and solely in the interest of, members and their beneficiaries. TRF is required by Indiana law to meet all rules applicable to a qualified plan under Section 401 of the Internal Revenue Code, in order to provide the ensuing tax advantages to its members. In addition, TRF is a trust, exempt from taxation under Section 501 of the Internal Revenue Code. TRF is also governed by Indiana statutes and administrative rules. See IC 5-10.2 and IC 5-10.4.

### **III. TRF Annuity Savings Account**

The Annuity Savings Accounts are bookkeeping accounts established for each member of TRF. The member's account is credited with the member's 3% contribution (whether paid by the member or "picked-up" by the employer). The member has limited investment direction to several alternative funds or may leave their account in the "guaranteed fund." The guaranteed fund affords the member a "risk free" protection on all contributions credited to that member's account, plus all previously credited interest (at an interest rate determined by the Board each year). These accounts produce an additional separate benefit from the fixed-formula employer-funded pension benefit.

### **IV. Description of Primary Statutory Investment Provision**

The Indiana General Assembly enacted the prudent investor standard to apply to the Board and govern all its investments. See PL 37-1996. In doing so, the General Assembly noted the following:

"Whereas, the general assembly also believes that a prudent diversification of investments by public retirement funds is an essential element of a stringent investment standard for such funds and is critical for the future; and Whereas, the general assembly finds that numerous actuarial studies of retirement funds in Indiana and other states have demonstrated that, due to the long term nature of the investments made by public retirement funds, diversification of such investments in a responsible manner reduces risk, increases income, and improves security for such funds, while a lack of diversification results in reduced income and increased risk to the retirement funds, while creating a substantial additional burden for the taxpayers who ultimately bear the burden of providing the assets for such funds in the absence of sufficient investment income; and Whereas, the general assembly desires to pass a diversification rule patterned after the stringent federal law applicable to private plans, which will provide that the trustees of each fund must diversify the investments of their fund so as to minimize the risk of large losses."

Thus, the primary governing statutory provision is that the Board must "invest its assets with the care, skill, prudence, and diligence that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character with like aims." The Board is also required to diversify such investments in accordance with prudent investment standards. See IC 5-10.4-3-10.

#### **V. Other Restrictions on Investments**

Other pertinent investment requirements in the Indiana statute include the following:

1. Fund investments must be held for the Fund by banks or trust companies under a custodial agreement or agreements. IC 5-10.4-3-13. All Custodians must be domiciled in the United States.
2. The Board may not engage in any prohibited transaction, as described in Section 503(b) of the Internal Revenue Code. IC 5-10.2-2-1.5(9).

#### **VI. Background of Investment Policy**

The Board has maintained an investment policy for many years. That policy has been amended and restated from time to time as the Board deemed appropriate, most recently as of August 31, 1999. The Board wishes to restate its policy to reflect those amendments, changes in applicable law, as well as other amendments it believes appropriate.

The Board intends this Policy to augment the governing laws, and supersede all prior statements of policy, principles and guidelines. This Policy is binding on all persons with authority over Fund assets, including Investment Managers, Custodians, Consultants, Staff, and the Board, as well as any other person who could have a relationship with the Fund.

#### **VII. Objectives**

All aspects of this statement should be interpreted in a manner consistent with the Fund's objectives. The objectives of the Fund have been established in conjunction with a comprehensive review of the current and projected financial requirements of the Fund. These objectives are:

- To have the ability to pay all benefit and expense obligations when due, at a reasonable cost to members and Indiana taxpayers.
- To maintain the purchasing power of the current assets and all future contributions by producing a positive real rate of return on Fund assets.
- To enhance the funded status of the plan with regard to the accumulated benefit obligation.
- To control the costs of administering the Fund and managing the investments
- To meet all statutory requirements of the State of Indiana.

## **VIII. Purpose of Policy**

The purpose of the Investment Policy is to:

- Set forth the investment policies which the Board judges to be appropriate and prudent, in consideration of the needs of the Fund, legal requirements applicable to the Fund, and to direct investment of the Fund's assets.
- Make a clear distinction between the responsibilities of the Board and the responsibilities of the investment managers selected by the Board to implement the Board's investment policy.
- Establish criteria against which the Investment Manager(s) are to be measured.
- Communicate the investment policies, objectives, guidelines, and performance criteria of the Board to the Staff, Investment Managers, Consultants, employers, members, and all other interested parties.
- Serve as a review document to guide the ongoing oversight of the investment of the Fund.
- Demonstrate that the Board is fulfilling its fiduciary responsibilities in the management of the investments of the Fund solely in the interests of members and beneficiaries of the Fund.

The Board does intend this Policy to be a dynamic document, and, as such, expects to review it periodically. The Board anticipates that changes will be made from time to time to reflect experience, investment product changes, benefit and structural changes, performance and economic conditions.

## **IX. RESPONSIBLE PARTIES AND THEIR DUTIES**

### **X. Board of Trustees**

The Board is the body of persons whose role is to oversee all aspects of the operation of the Fund IC 5-10.4-3-6. The Board is appointed by the Governor for a four year term, pursuant to IC 5-10.4-3-6 and IC 5-10.4-3-2, and consists of six (6) trustees. One trustee is the director of the budget agency or his designee. At least two Board members must be members of the Fund. The Board members are fiduciaries of the Fund. Their responsibilities with respect to the assets of the Fund include completing each of the duties below as a prudent investor:

- Set the policies, objectives, and guidelines for the investment of the assets of the Fund.
- Study issues affecting the investment of the Fund so as to make educated and prudent decisions concerning this Policy.
- Select qualified professionals to assist in the implementation of this Policy.

- Evaluate the Fund's performance and compliance with this Policy and applicable state and federal laws.
- Evaluate performance of investment professionals and staff.

#### **XI. Investment Staff of Fund**

The Staff are those persons employed by the Fund. The Board has the authority to set compensation of the Staff. Staff duties are to administer the Fund in line with the policies and decisions of the Board and the provisions of governmental law and to provide input and recommendations so that issues can be studied fully prior to any Board decision. In addition, Staff is responsible for interacting with the legislature, serving the needs of Fund members, and managing the Fund's relationships with outside professionals and other constituencies.

#### **XII. Executive Director**

The Executive Director, a member of the Staff, is appointed by the Governor and must be a member of the Fund. The Executive Director acts on behalf of the Board, and is responsible for performing duties as assigned by the Board, as well as for receipt of payments and deposits to the Fund, and payments from the Fund.

#### **XIII. Investment Manager**

An Investment Manager is a person(s), firm, corporation, bank or insurance company who is retained to manage a portion of the assets of the Fund under specified guidelines. Such Investment Managers will be registered as investment advisors under the Investment Advisors Act of 1940 and Securities Exchange Commission Acts, unless exempted from registration by the SEC (i.e., banks and insurance companies and affiliates).

#### **XIV. Custodian**

A Custodian for the Fund is a bank or trust company, which is retained by the Board. A Custodian may be authorized to (1) hold securities and other investments in the name of the Fund, in the name of a nominee of the Custodian, or in bearer form; (2) collect and receive income, interest, proceeds of sale, maturities, and investments; deposit all these receipts in a custodian account or checking account as instructed by the Board; and reinvest these receipts as directed by the Board; (3) maintain accounting records and prepare reports which are required by the Board and the State Board of Accounts; (4) perform other services for the Board as are customary and appropriate for custodians; and (5) if retained, to conduct any analysis required by the Board.

#### **XV. Consultants**

Consultants are persons or firms who are retained by the Board and are responsible for providing advice on the investment program consistent with and within the context of the contracted services to the Fund, based upon their expertise and their analysis of the issues under consideration.



## **XVI. CODE OF ETHICS**

### **XVII. Fiduciary Responsibility**

The members of the Board recognize that they serve as fiduciaries of the Fund. One of their primary responsibilities is the prudent investment of Fund assets. Thus, the Board shall exercise the care, skill, prudence and diligence that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with like aims. The Board must also diversify the investments of the Fund in accordance with prudent investment standards. IC 5-10.4-3-10. The Board has a duty of undivided loyalty, and must be impartial in the exercise of such duty, to the beneficiaries of the Fund, as all Fund assets must be used for the exclusive benefit of the Fund's covered members and their beneficiaries. No part of the corpus or income may be used for or diverted to any purpose other than for the "exclusive benefit" of the members or their beneficiaries. IC 5-10.2-2-1.5. The Board may not engage in any transactions prohibited by Section 503(b) of the Internal Revenue Code. IC 5-10.2-2-1.5(a). Board members or anyone acting on their behalf must comply with these provisions.

### **XVIII. Compliance with Code of Ethics**

Board members recognize that they are governed by certain provisions of the Indiana Code of Ethics. Because they believe that public confidence in the Board's integrity is essential not only for members of the Fund, but also for the public and taxpayers of the State of Indiana as well, they wish to ensure that their actions conform not only with the letter of the law but also with the spirit of the law.

As to the Board, the Indiana Code of Ethics includes the following:

No appointee shall accept any compensation from any employment, transaction, or investment which was entered into or made as a result of material information of a confidential nature. See IC 4-2-6-6.

As to Staff, the Indiana Code of Ethics sets forth specific guidelines that all State employees, including Fund staff, are to observe. See IC 4-2-6.

As to any other person (including, but not limited to consultants, custodians, investment managers), the Indiana Code of Ethics provides:

It shall be unlawful for any person, other than employees performing their duties in making payments to employees as provided by law, to pay, or offer to pay, any employee any compensation for the performance of his official duties. See IC 4-2-6-5. Compensation includes any money, thing of value, or financial benefit.

#### **A. Conflict of Interests Rules**

Board members recognize that all Fund transactions and selections are to be based on the integrity and competence of the parties with whom the Fund is dealing and upon financial merit and benefit to Fund members and their beneficiaries, and not on personal relationships. Board members shall never act where there may be a conflict of interest or appearance of conflict of interest. They realize they occupy special positions of fiduciary trust and confidence such that each member must studiously and conscientiously avoid any

reasonable appearance of conflict. A conflict of interest is understood to be presented in a situation wherein a relationship exists which could reasonably be expected to diminish independence or judgment in performance of official responsibilities as a Board member. Accordingly, a Board member shall not engage in conduct that constitutes or involves a conflict of interest. It is the Board member's duty to determine if a potential conflict of interest exists, to avoid the conflict, if possible, or, where applicable, to disclose a conflict. If a Board member determines that a conflict of interest or potential conflict of interest exists, that individual shall have an obligation to recuse themselves from participating in the matter. The Board member shall disclose the reason for any such recusal.

- Statutory Provisions

Title 5-10.4 of the Indiana Code governs the Fund and specifically addresses conflicts of interest as follows:

- (a) Except as otherwise provided or as may arise due to their status as members of the Fund, no trustee or employee of the board may have any direct interest in the income of any investment made by the board nor may receive any pay or emolument for services connected with any investment made by the board.
- (b) No trustee or employee may become in any manner an obligor for money loaned by or borrowed from the fund. See IC 5-10.4-3-15.

A trustee or employee recklessly violating this provision would commit a Class A misdemeanor. See IC 5-10.4-3-16.

- Voting

Board members should not participate in a discussion or vote on a matter in which they have a direct or indirect significant financial interest. However, this prohibition does not arise in connection with a matter which would have an insignificant economic effect on any interest of the Board member, or which affects the member only as a member of the general public or of a subgroup of the general public, such as members of the Fund as a whole.

- Disclosure

1. Any person who serves on the Board shall fully disclose any substantial interest in any entity in which an investment has been made with monies of the Fund.
2. Board members shall disclose any significant business relationship they have with any vendors or prospective vendors serving or considered for service to the Fund.

## **XIX. Specific Board Rules of Conduct**

In furtherance of the general principles stated above, the Board has adopted the following specific rules.

### Contact with Investment Managers

It is the Board's policy that all contact with Investment Managers or others seeking a business relationship with the Fund should be directed to the Executive Director and Staff, not to individual Board members. For example, during a manager, consultant or other professional search process, it is the Board's policy that no contact with prospective bidders and individual Board members is appropriate. However, the Board recognizes three exceptions to this general rule. First, this rule is not applicable to circumstances arising in the ordinary course of business of an individual that is unrelated to the individual's status as a Board member. Second, this rule is not applicable to contacts relating to Board business with Investment Managers and Consultants with whom the Board has an existing fiduciary relationship. For example, Board members are encouraged to contact an existing Investment Manager with any questions or concerns they might have with respect to a specific investment directed by that Investment Manager. Third, any other casual incidental contact with an existing or prospective Investment Manager or Consultant that a Board member has, not directed to specific Fund matters, should be disclosed to the Executive Director.

### Gifts

A Board member, or the spouse or unemancipated child of a Board member shall not accept for personal use any gifts, favors, services, entertainment, food or drink from a person or business that is seeking or actually has a business relationship with the Fund, or is seeking to influence an action by the Board member in his or her official capacity. However, it is understood that this prohibition is not applicable to circumstances arising in the ordinary course of business of an individual that is unrelated to his or her status as a Board member. Further, food or drink provided for and consumed at: 1) a public meeting to which at least twenty-five (25) individuals are invited; 2) an event or reception or other gathering for public officials that is not arranged to solicit Fund procurement of goods or services; 3) or a formal educational program that the Board member is attending to assist him or her in performing official does not violate this section.

### Speaking Engagements

A Board member may not accept any expenses, reimbursement, or honorarium for any speeches or presentations made in his or her capacity as a Board member. This rule does not apply to circumstances where the individual is speaking or presenting in a capacity unrelated to Board membership or as to which Board membership is simply recognized as a part of such member's professional experience. When Board members are speaking on behalf of the Fund, the topic and speech notes should be reviewed and approved by the Executive Director.

## **XX. Conferences and Educational Activities**

Board members are encouraged to attend appropriate educational conferences and meetings to assist them in performing their duties. It is the Board's policy to reimburse Board members for expenses related to such activities. The Executive Director will serve to coordinate attendance and administer reimbursement, subject to any required procedure.

## **XXI. Responsibilities of Investment Managers and Consultants**

In order to accomplish these objectives, each Investment Manager and Consultant retained by the Fund shall be notified in writing of the Board's Code of Ethics and the related Conflict of Interest laws of the State of Indiana, and of the Board's adoption of this Code. All Investment Managers shall strictly conform to the Board's Code of Ethics. Any suggestion or offer to deviate from these provisions made by a Board member or Staff member shall be reported by the Investment Manager or Consultant, in writing, to all members of the Board.

The Board recognizes that Investment Managers and Consultants have every right as citizens to participate in the political process both individually or corporately. However, the Board believes that it is inappropriate and improper for members of the Board to solicit contributions or support of specific candidates from any Investment Managers, Consultants or Staff. Any such incidents should be reported, in writing, by the Investment Manager or Consultant to all members of the Board.

All Investment Managers, Consultants and other persons retained in any capacity which have fiduciary responsibilities are expected to abide by the provisions of the Board's Code of Ethics.

## **XXII. INVESTMENT POLICY GUIDELINES**

### **XXIII. Asset Allocation Guidelines**

The Board recognizes that the allocation of assets, particularly the broadly-defined mix between stocks and bonds, is the most important determinant of investment rates of returns over long periods of time. The procedure for determining the allocation will consider the relevant characteristics of the liabilities and the potential assets of the Fund. An asset allocation and liability study will be conducted no less than every three years. The study will analyze the expected returns of various asset classes, projected liabilities, the risks associated with alternative asset mix strategies and their affect on the projected market value of assets, funded status and contributions of the Fund.

Based on the most recently completed study (September, 2006), the Board has established an asset allocation that is listed in Appendix I. (This appendix also lists all prior asset allocations since the passage of a Referendum in 1996 allowing the Board to diversify.)

Within each asset class, the Board in its discretion may establish subcategories, and the Board also may establish the mix between active Investment Managers and passive index Investment Managers. The current asset class subcategories and their respective benchmarks are listed below.

<b><u>Asset Class</u></b>	<b><u>Sub-Asset Class</u></b>	<b><u>Benchmark</u></b>
<b>Domestic Equity:</b>	Broad Market Index	Russell 3000
	Large Cap Index	S&P 500 and/or Russell 1000
	Large Cap Enhanced Index	S&P 500 and/or Russell 1000
and/ Value	Large Cap Value	S&P 500 Value or Russell 1000
and/ Growth	Large Cap Growth	S&P 500 Growth or Russell 1000
	Mid Cap Core	S&P 400
Value	Small-Mid Cap Value	Russell 2500
Growth	Small-Mid Cap Growth	Russell 2500
Value	Small Cap Value	Russell 2000
Growth	Small Cap Growth	Russell 2000
<b>International Equity:</b>	International Index	MSCI EAFE and/or MSCI ACWI ex-
US		
and/or	International Enhanced Index	MSCI EAFE
us		MSCI ACWI ex-
and/or	International Active	MSCI EAFE

		MSCI ACWI ex-us
<b>Domestic Fixed Income:</b>	Core	LB Agg. Index
	Core – Opportunistic	LB Agg. Index
<b>Private Equity:</b>	Discretionary Fund of Funds	15% Return
<b>Domestic Real Estate:</b>	Core	6% Return
	Core Opportunistic	8% Return
<b>Alternative Investments:</b>	Global Tactical Asset Allocation	Custom Benchmark

#### **A. Rebalancing of Asset Allocation Guidelines**

The Board recognizes that from time to time the asset mix will deviate from the targeted percentages due to market conditions. A range has been established for each asset class to control risk and maximize the effectiveness of the Fund's asset allocation strategy, while avoiding unnecessary turnover at the security level.

The percentage allocation to each asset class on a market value basis should be reviewed by the staff each quarter. When an asset class is outside of its allowable range, a reallocation should be made to rebalance that asset class back into the allowable range considering current market conditions.

Where possible, cash flow to or from the Fund should be used to rebalance back to the targeted percentage as much as possible, since this avoids unnecessary turnover of securities. Where transfers between accounts are required managers should be notified in advance, if possible, of the amount and timing of any transfers to or from their accounts.

#### **XXIV. Time Horizon**

The Board acknowledges that fluctuating rates of return characterize the securities markets, particularly during short-term periods. Accordingly, the Board views interim fluctuations with an appropriate perspective.

Recognizing that short-term fluctuations may cause variations in the total portfolio's performance, the Board encourages each investment manager to develop long-term investment strategies consistent with the guidelines contained in this Investment Policy Statement. A five year time period reflects the Board's emphasis on the long term, although significant deviations from performance objectives will be monitored for appropriate action.

#### **XXV. Performance Evaluation Factors for Total Fund**

The key factors to be used in the analysis of the investment performance of the total Fund include:

- The progress on the benefit funding requirements of the Fund.

- Investment rate of return and volatility of the Fund, compared with a weighted average of market indexes, which best describe the Fund's allocation.
- Investment rate of return of the Fund, compared with other large private and public pension funds with special emphasis on other large public funds.

## **XXVI. INVESTMENT MANAGER GUIDELINES**

### **XXVII. General Guidelines for Investment Managers**

Each Investment Manager retained to manage a portion of the assets (the Investment Manager's "Portfolio") of the Fund shall be aware of and operate within this Investment Policy and governing Indiana statutes. Subject to the guidelines in this Section and the policies documented in this Statement, any Investment Manager retained by the Fund is to have full discretionary investment authority over the assets said Investment Manager is responsible for managing. Each manager will therefore submit to the Fund its own product guidelines specific to the portfolio it manages. Approval of the portfolio specific guidelines shall be evidenced by the acceptance and signature of the Chief Investment Officer.

As fiduciaries of the Fund, all Investment Managers (regardless of type of investment) will discharge their duties solely in the interests of the Fund's members and beneficiaries and with the care, skill, prudence, and diligence that an expert would use on his/her own behalf. In addition, the Investment Managers, other than Investment Managers covered by the Investment Policy for Private Equity Investments, Section XIII, and the Investment Policy for Real Estate, Section XVI, shall observe the following rules:

Securities Trading. Each Investment Manager is to immediately send copies of each transaction record to the Fund's Custodian(s), and any designated agent of its Custodian(s). Each Investment Manager is further required to reconcile the account(s) under its management on a timely basis each month with the Custodian(s). Each Investment Manager is responsible for complying fully with the Fund's policies for securities trading and selecting brokerage firms.

Acknowledgments of Legal Compliance. Each Investment Manager retained by the Fund must be a person, firm, or corporation registered as an investment adviser under the Investment Advisors Act of 1940; a bank as defined in such Act; or an insurance company qualified to do business in more than one state, and must acknowledge its fiduciary responsibility in writing. SEC registered firms will be expected to provide a copy of the SEC ADV Form Section II on an annual basis.

Acknowledgments of Receipt. All Investment Managers shall acknowledge in writing their receipt of this Policy and their agreement to abide by its terms. All Investment Managers shall have an affirmative duty to bring suggestions for modification or change of the Policy to the Board.

Ethics Policy. All Investment Managers will provide the Fund with a copy of their respective ethics policy.

Fiduciary Liability Insurance. Each Investment Manager will obtain fiduciary coverage in an appropriate amount. The fiduciary coverage must cover a loss resulting from a breach of fiduciary duty in providing or failing to provide professional services to the Fund. In some cases, fiduciary coverage may be established through errors and omissions (E&O) or professional liability policies (including, for some Investment Managers, a "blanket bond" if the bond also provides coverage for fiduciary liability), as long as those policies are specifically written to cover fiduciary breaches themselves or include a specific fiduciary liability endorsement or rider.

Each Investment Manager shall annually provide written evidence of such coverage. The Executive Director may approve alternative fiduciary liability insurance arrangements, if in the judgment of the Executive Director, Chief Investment Officer, and Fund legal counsel, the alternative insurance arrangements provide substantially the same protection to the Fund.

Errors and Omissions Coverage. Each Investment Manager will obtain coverage for errors and omissions to cover a loss due to a mistaken or negligent act or omission (without any exclusions for benefit plans that would exclude services the Investment Manager provides for TRF from coverage) in an appropriate amount. Each Investment Manager shall annually be required to provide written evidence of such coverage.

The Executive Director may approve alternative errors and omissions coverage, if in the judgment of the Executive Director, Chief Investment Officer, and Fund legal counsel, the alternative insurance arrangements provide substantially the same protection to the Fund.

Fidelity Bond. Each Investment Manager will obtain a fidelity bond, which covers loss from acts of dishonesty, theft, or negligence, in an appropriate amount. Each Investment Manager shall annually be required to provide written evidence of such coverage.

The Executive Director may approve alternatives to a fidelity bond, if in the judgment of the Executive Director, Chief Investment Officer, and Fund legal counsel, the alternative insurance arrangements provide substantially the same protection to the Fund.

Proxy Voting. Each Investment Manager will abide by the Fund's Proxy Voting Policy as stated in Section 9 of this Statement. Each Investment Manager will provide at least annually a report of proxy voting activity to the Fund consistent with the requirements of Section 9.

Conflicts of Interest. An Investment Manager shall be subject to the applicable provisions of Section III of this Statement. An Investment Manager through its actions on behalf of the Fund shall not invest any part of the Fund with itself or with any person or entity with which or in which it has any economic interest, unless such Investment Manager receives prior written approval from the Board.

This limitation shall be construed so as to avoid any possibility of self-dealing or conflict of interest. In addition, no Investment Manager, through its actions on behalf of the Fund, shall act or receive compensation as a broker, dealer, underwriter, or principal whether directly or



through a related or an affiliated entity, unless such Investment Manager receives prior written approval from the Board.

Prohibited Securities and Transactions. Except as otherwise authorized by the Board, as evidenced by the approval of an Investment Manager's portfolio specific guidelines, the following transactions shall be prohibited:

- Short sales of any kind
- Repurchase agreements that may create any kind of leverage in the portfolio. (Repurchase agreements as cash equivalents are permitted.)
- Purchases of letter or restricted stock
- Buying or selling on the margin
- Any transactions giving rise to unrelated business taxable income (excluding current holdings)
- Any transaction that would be a "prohibited transaction" under the Internal Revenue Code Section 503
- Purchases of precious metals
- Purchases of commodities

Commingled and Pooled Investments. In accordance with IC 5-10.2-2-2.5, Investment Managers may, with the express written permission of the Chief Investment Officer of the Fund, invest in commingled or pooled funds that otherwise comply with the guidelines in this Policy.

Correction of Violations. In the event a violation of the guidelines occurs, unless otherwise approved by the Executive Director in writing, based upon a determination of the best interests of the Fund, the violation:

- Shall be corrected immediately by sale as soon as practicable following detection and notification, unless the Chief Investment Officer has agreed in writing to a correction which does not result in immediate disposition or sale
- Shall result in the reimbursement of the Fund by the Investment Manager for any losses which may have been incurred due to the violation
- Shall result in the Fund retaining any gains which are realized from the violation
- May be grounds for termination by the Board

## **XXVIII. Reporting Procedures for Investment Managers**

The Investment Manager shall:

- Prepare a quarterly report to be delivered to the Staff, which includes those items requested by the Fund, in the format requested by the Fund. These reports should cover any changes in the firm's structure, professional team or product offerings; a review of recent and anticipated investment activities; an analysis of the major changes which have occurred in the investment markets and in the Portfolio in particular since last report; a summary of the key characteristics of the Portfolio; and other matters as requested by the Fund from

time to time. Periodically, the Staff may provide the Investment Manager with a detailed description and format for these reports.

- Make a presentation to the Board or its designated committee when requested by the Board, describing the professionals, the investment process employed for the Fund's Portfolio under the Investment Manager's responsibility, recent performance of the Portfolio, current investment strategy and outlook, and any other related issues as requested by the Board or its designated committee.
- Meet regularly with the Staff to discuss the management of the Portfolio, new developments and any other related matters.
- Advise the Staff immediately and in writing if any of the following events occur within the Investment Manager organizations:
  - a loss of one or more key people
  - a significant change in investment philosophy
  - a new portfolio manager(s) or account manager(s) on the Fund's account
  - a change in ownership or control (whether through acquisition, disposition, spin-off, merger, consolidation, or otherwise) or in business focus of the Investment Manager
  - loss of a significant client relationship( s)
  - any other event which could be judged to or deemed to adversely impact to a significant degree the management, professionalism, integrity or financial position of the Investment Manager

## **XXIX. Performance Measurement**

A time-weighted return formula (which minimizes the effect of contributions and withdrawals) should be utilized. The services of an outside, independent consulting firm providing performance measurement and evaluation may be retained. Investment Managers will be expected to comply with the CFA Institute Performance Presentation Standards in calculating and reporting their investment performance. The Fund, and any firms retained by the Fund to calculate investment performance, will also adhere to the CFA Institute Standards.

### **A. Performance Evaluation Factors for Investment Managers**

Rates of return will be evaluated on both a gross and net of fee basis. In order to provide more definition and consistency, one year, three year, five year, and rolling three and five year periods will be used. Rolling periods shall be defined as a three (or five) year period beginning with the earliest reasonable date and including subsequent three (or five) year periods each beginning one year later until the ending date is the end of the current period. If needed to further evaluate investment performance, other time periods may be employed.

Any of the following standards may be used as a guideline for the evaluation of the investment performance of the Investment Managers:

- Gross of fee rates of return ranking at or above the median of an appropriate universe or style peer group of investment managers.
- Net of fee rates of return exceeding an appropriate market index benchmark.
- Risk - adjusted rates of return exceeding an appropriate market index benchmark.
- Volatility consistent with the assigned asset class, and relative to the appropriate market index benchmark.

### **XXX. Watch List Procedures**

The “Watch List” procedures are established to describe the conditions leading to an investment manager being placed on the list, and the conditions that lead to a manager being removed or terminated. The purpose of the Watch List is to provide an objective plan to assist the Board in deciding when a manager relationship should be terminated.

Conditions considered by the Board in determining whether an Investment Manager should be listed:

#### **Qualitative**

- Firm changes ownership structure
- Key people leave firm
- Manager changes strategy it was hired to implement
- Manager is involved in material litigation or fraud
- Material client servicing problems
- Deterioration of financial condition
- Any other event which could be judged to or deemed to adversely impact to a significant degree the management, professionalism, integrity or financial position of the Investment Manager

#### **Quantitative**

- Three year total fund return (gross of fees) that is less than the manager’s benchmark.
- Bottom quartile performance relative to peer group for a 12 month period.

#### **Conditions for Removal from List or Termination**

If extraordinary organizational change or consistent underperformance occurs, all related issues will be rigorously evaluated by consultant and staff. Based on this analysis, a recommendation will be made to the Board as to whether the manager should be terminated, removed from the watch list or remain for a specified time period.

### **XXXI. Manager Selection Procedure**

The Board has responsibility for selecting investment managers. The Board's intent is to follow a process that embodies the principles of procedural due diligence. Accordingly, when selecting investment managers, the Board will:

- Retain an investment consultant
- Retain a “prudent expert” (a bank, insurance company, or investment advisor as defined by the Registered Investment Advisors Act of 1940).
- Follow a due-diligence process so as to avoid selecting managers on an ad-hoc basis. The due diligence process, at a minimum, will involve analyzing investment manager candidates in terms of certain:

**Qualitative Characteristics**, such as key personnel, investment philosophy, investment strategy, research orientation, decision-making process, and risk controls.

**Quantitative Characteristics**, such as CFA Institute-compliant composite return data, risk-adjusted rates of return (e.g., Sharpe Ratios and Information Ratios), and certain portfolio characteristics, such as  $R^2$  in relation to an appropriate market index.

**Organizational Factors**, such as type and size of firm, ownership structure, client-servicing capabilities, record of gaining and keeping clients, and fees.

#### **A. Manager Termination**

In the event a manager is terminated by the Board, the Board, at its discretion, may take all actions necessary and appropriate to move and reinvest the assets that were held by such manager. Action by the Board in this regard is not a contravention of the Fund's procurement policy.

### **XXXII. TRADING AND BROKERAGE POLICY**

#### **XXXIII. Introduction**

The Board intends to fulfill its responsibility for the evaluation and management of transaction costs for the exclusive benefit of members and beneficiaries. To assist in accomplishing these duties, this trading and brokerage policy has been implemented by the Board.

#### **XXXIV. Basic Principles**

The Board requires that these principles guide all transactions for the Fund:

Best execution and lowest cost, (including commission costs and market impact) and providing benefits exclusively for members and beneficiaries of the Fund must apply to trades.

Efforts to reduce trading costs, in terms of both commissions and market impact, provided the investment returns of the Fund are not jeopardized, will be ongoing.

The Board intends there to be a prohibition on any self dealing on the part of any brokerage firm, including any with such a firm's broker affiliate, without specific prior authorization.

**A. Basic Criteria for Selection of Brokerage Firm**

The primary responsibility of the Board is to act as a fiduciary to the members and beneficiaries of the Fund. The Board requires that all transactions of publicly traded securities be effected through brokerage firms or exchanges, regardless of location, in order to obtain the best execution and lowest cost of the transaction.

Subject to any direction from the Board, each Investment Manager will be responsible for the selection of brokerage firms, or automated trading systems through which trading will be completed for the Fund. Each Investment Manager is also responsible for conducting all appropriate and necessary due diligence on the brokerage firms it selects. Their selection must in all cases be for the benefit of the Fund's members and beneficiaries and should strive for best execution with lowest cost on trades.

**XXXV. Directed Brokerage/Commission Recapture Policy**

The Board does retain the right to direct brokers and enter into brokerage commission recapture agreement(s). Accordingly, the Board has developed the following policy guidelines to ensure that any directed brokerage or commission recapture policy is a prudent policy that best serves the interests of the Fund's participants and beneficiaries:

1. The objective of the policy is to achieve both commission cost savings and "best execution."
2. Any directed commission brokers will be selected through a process directed by Staff.
3. The percentage of each investment manager's portfolio to be directed to the Board's directed commission broker(s) shall be mutually agreed upon in advance between each investment manager and Staff. Staff shall seek the advice and counsel of the Board's investment consultant during this process. The objective will be to select a percentage amount that generates substantial commission savings, without hindering the investment manager's abilities to execute investment strategies that "add value."
4. Directed commission brokers will provide Staff with periodic reports that document the date and commission amount associated with every directed trade, by investment manager. In this manner, Staff will be able to monitor the overall directed brokerage program, the services of the directed commission broker, and the progress each investment manager is making toward any directed commission goal.
5. Commission recapture services will be utilized, where feasible, to defray costs and benefit the plan participants, subject to the manager's "best execution" efforts.
6. The Board intends there to be a prohibition on any self dealing on the part of any brokerage firm, including any with such a firm's affiliate, without specific prior authorization.

**XXXVI. Review/Evaluation**

At least annually, the Board will review all transactions and arrangements, if any, for compliance with these policies through an annual Trading Cost Analysis. The Investment

Managers and Custodian providing services shall provide any information necessary or helpful to this review.

**XXXVII.        Disclosure**

In addition, each Investment Manager shall report at least annually on brokerage firms they are using and the terms of those relationships. This disclosure must cover all components of that relationship, including but not limited to, payment for order flow, soft dollars, covered expenses, and the nature of the broker selection process.

**XXXVIII.        GUIDELINES FOR THE CUSTODIAN**

The Board recognizes that accurate and timely completion of custodial functions is necessary for effective investment management and accurate records. The custodian is a fiduciary as to the assets placed with them by the Fund. The Board identifies the following as responsibilities of the custodian(s) for the segments of the Funds for which the custodian is responsible:

1.     Provide complete custody and depository services for the designated accounts.
2.     Provide for prompt investment of any cash to avoid uninvested amounts.
3.     Implement in a timely and effective manner the investment actions as directed by the investment manager(s).
4.     Receive all income and principal realizable and properly report transactions in periodic statements.
5.     Provide monthly and annual accounting statements as well as on-line access accounting for the Fund, including all transactions; these should be based on accurate security values both for cost and market value. These reports should be provided within ten days of the close of the period.
6.     Report to the Staff situations where security pricing is either not possible or subject to considerable uncertainty.
7.     Distribute to the investment manager(s) in a timely manner all proxy voting materials.
8.     Provide assistance to the Board and Staff, to complete such activities as the annual audit, transaction verification and other issues.
9.     As requested by Board, provide performance measurement and portfolio analytics for the Fund, consistent with CFA Institute standards.
10.    When directed by the Board, and pursuant to a separate, written agreement for securities lending service, implement, in a fair and equitable manner, a securities lending program for the Fund, and report fully on all aspects of its operation and returns.
11.    The custodian shall cooperate fully with all reasonable requests for documents and records made by the Board or a consultant designated by the Board. The Board (on its own or through its consultant) shall periodically review the custodians, including but not limited to, services provided, services available, charges and fees, and reports.

12. The custodian shall conform to all provisions in its contract with the Fund.

## **XXXIX. SECURITIES LENDING POLICY**

### **A. Background**

IC 5-10.2-2-13(d) provides that the Board may authorize a custodian to enter into a securities lending program agreement under which securities held by the custodian on behalf of the Fund may be loaned. The purpose of such a program is to provide additional revenue for the Fund. IC 5-10.2-2-13(d) provides that collateral initially in excess of the total market value of the loaned securities must be pledged by the borrower, and must be maintained at no less than the total market value of the loaned securities.

### **B. General Statement With Respect to Board's Intent**

The Board intends to maintain a securities lending program, as the Board believes it provides a means of enhancing the overall Fund performance. The investment objective for the securities lending program is to generate incremental income within a high quality investment program that safeguards the return of principal, maintains adequate daily liquidity, ensures diversification of the cash collateral portfolio and tightly controls exposure to fluctuating interest rates. The Board will evaluate the income attributable to the program and the risks inherent in the program. The Board expects each custodian who has been authorized to enter into an agreement to evaluate at least annually the agent selected by the custodian and the Board, to offer suggestions with respect to any possible improvements in the program, and to monitor the results of the program (e.g., income, costs associated with the program, issues that arise with respect to the program) and report to the Board as directed.

### **C. Method of Implementation**

The specifics pertaining to any securities lending program shall be detailed in a separate Securities Lending Agreement. Upon request of the Fund, the custodian may provide, or may arrange for an agent or subcustodian to provide, a securities lending program to be operated in accordance with this Policy. Any agent or subcustodian to be used by the custodian to provide a securities lending program to the Fund must be approved by the Fund in advance and in writing, and such approval may be revoked by the Fund, for any reason, upon five (5) days' written notice to the custodian. In order to engage in securities lending on the Fund's behalf, the custodian's subcustodian will have the care and custody of and will perform any custodial services incident to the securities loaned and to be loaned. The custodian shall be responsible for and shall ensure that any subcustodian engaging in securities lending services for the Fund shall adhere to and be bound by this Policy. All costs associated with the use of a subcustodian shall be borne by the custodian. For purposes of this Policy, the "Securities Lending Custodian" shall refer to the custodian or its subcustodian, as appropriate, with respect to the performance of securities lending services. The Securities Lending Custodian shall agree to keep all assets of the Fund that are subject to the Securities Lending Custodian's custodial care in a segregated account.

Additional implementation requirements include the following:

- The Securities Lending Custodian shall allocate loan opportunities among its securities lending participants, including the Fund, in a reasonable and equitable manner.
- The Securities Lending Custodian shall enter into a borrowing agreement with each borrower of the Fund's securities setting forth terms not inconsistent with these Guidelines or any other agreement between and among the Fund and its custodian and/or its Securities Lending Custodian. All loans shall be made (i) on behalf of and solely for the benefit of the Fund; (ii) only to a borrower that does not have, and no affiliate of which has, any discretion, investment authority or control, or any investment advisory responsibility with respect to the securities being loaned; and (iii) on terms that are at least as favorable to the Fund as an arm's length transaction with an unrelated party would be. On the day of the loan, the Securities Lending Custodian shall deliver to borrower or release through a clearing agency the securities to be loaned and contemporaneously therewith, the Securities Lending Custodian shall receive from the borrower or through a clearing agency all collateral required to secure the loan.
- Income earned by the Fund in connection with the Securities Lending Program shall be credited to the Fund's custodial account no less frequently than once a month.
- "Distributions" shall refer to all dividends and other distributions made on or with respect to any loaned securities, including but not limited to: (i) cash; (ii) stock or property dividends or distributions; (iii) securities received as a result of split-ups of the loaned securities and distributions with respect thereto; (iv) interest payments; (v) subscription rights; and (vi) all rights to purchase additional securities. The Fund shall be entitled to receive all Distributions made by an issuer with respect to any loaned securities to the same extent as if the securities had not been loaned. The Fund understands that it does not retain the right to vote any securities that are still on loan as of a record date for determining voting rights. All Distributions on the loaned securities shall be credited to the Fund's account on the payment date, and the Securities Lending Custodian shall assume the responsibility of collecting such Distributions from the borrower or other recipient.
- The Fund shall be entitled to no less than eighty percent (80%) and the Securities Lending Custodian shall be entitled to no more than twenty percent (20%) of (i) the total Premiums paid by the borrower in a loan of securities against Securities Collateral; and (ii) the total Yield, after deducting the Rebate, in a loan of securities against Cash Collateral.
- The Fund shall direct the investment manager of the securities to notify the custodian of any sales by no later than the trade date to permit the custodian to effect timely return of loaned securities prior to or on the settlement date.
- In order to verify that the procedures set forth in this Policy are being followed, the Securities Lending Custodian shall cooperate fully with all reasonable requests for documents and records made by the Fund and/or an independent certified public accountant selected and retained by the Fund to audit securities lending activities.
- In the event of a conflict between this Policy and any provisions of any contract



between the Fund and the Securities Lending Custodian to which this Policy becomes a part, the provisions of this Policy shall prevail.

#### **D. Risk Controls**

Any Securities Lending Custodian shall agree in writing, among other things, to 100% indemnification of the Fund for any loss sustained as a result of borrower default, borrower's failure to pay over Distributions, borrower's failure to timely deliver or return collateral or the loaned securities, and overnight market risk; provided, however, that the Fund will bear the market risk of a decrease in the value of collateral acquired by the investment of Cash Collateral. Upon notification of default by the borrower, which shall be reported immediately to the Board in writing, the custodian shall take such actions as are prudent, necessary and appropriate to use the collateral to acquire replacement securities of the exact same type and kind as the securities which were loaned to the borrower. Any inability to acquire such securities shall be reported to the Fund and to the investment manager immediately.

The custodian and/or securities lending sub-agent is responsible for conducting all appropriate and necessary due diligence on the borrowers and potential borrowers. The Securities Lending Custodian shall propose loans of the Fund's securities only to borrowers meeting the Securities Lending Custodian's customary standards of creditworthiness. The Securities Lending Custodian shall formally review the creditworthiness of the borrowers approved by the Fund no less frequently than annually, and shall remove any borrower no longer meeting the Securities Lending Custodian's customary standards of creditworthiness. The name of borrowers and potential borrowers shall be updated and provided to the Board promptly following the end of each calendar quarter.

The Securities Lending Custodian shall be responsible for receiving acceptable collateral from the borrower to secure each securities loan. "Acceptable Collateral" shall refer only to the following forms of collateral:

- "Cash Collateral," meaning collateral in the form of cash and evidenced by a certified check, bank cashier's check, wire transfer or, if the loaned securities are delivered to the borrower through an approved central depository system, funds delivered through such depository, including all accounts or instruments in which any such checks or funds are deposited or invested, any proceeds of the foregoing and any increases or decreases to the cash collateral resulting from the marking to market adjustments;
- "Securities Collateral," meaning collateral consisting of securities issued, or guaranteed as to principal and interest, by the United States Government, its agencies or instrumentalities, together with all present and future proceeds therefrom including all accrued and unpaid interest, and any and all distributions made by the issuer on or with respect thereto, and including any increases or decreases thereto resulting from the marking to market adjustments; and
- Any combination of Cash Collateral and Securities Collateral agreed upon by the Securities Lending Custodian and a borrower.

The Securities Lending Custodian shall require any borrower to deliver Acceptable Collateral valued at the inception of the loan as at least equal to 102% of the Market Value

of the loaned fixed income securities and 105% of the Market Value of the loaned equity securities. At the close of the market each day, the Acceptable Collateral shall be “marked to market,” meaning that Market Value of the loaned securities shall be determined, and if the Market Value of the collateral securing the loan is 100% or less of the Market Value of the respective loaned securities for that day, the borrower shall be required to deliver additional collateral to bring the value back to at least 102% for fixed income securities and 105% for equity securities, by the close of trading on the next business day. Cash Collateral, for purposes of these collateral requirements, shall be valued at either the amount of cash deposited or the purchase price of the securities purchased with such cash. In no event shall the Acceptable Collateral be less than as required by Indiana Code §5-10.2-2-13(d).

Securities shall not be loaned in excess of forty percent (40%) of the market value of the Fund’s assets (not to be taken on an individual manager account-by-account basis) under the care of the custodian, marked to market on a day-to-day but not on an intra day basis.

All investments shall be subject to the prudent investor rule.

#### **E. Cash Collateral Investment Guidelines**

**Permissible Investments.** The Securities Lending Custodian on behalf of the Fund may invest the cash received as collateral to secure the loan of the Fund’s securities (the “Cash Collateral”). The Securities Lending Custodian shall exercise reasonable care, skill, diligence and prudence in connection with such investments. Any securities acquired in violation of the Cash Collateral Investment Guidelines shall be sold no later than the day following detection, and the Securities Lending Custodian shall reimburse the Fund for any losses and the Fund shall retain any gains. Such Cash Collateral shall be invested only in the following investment instruments (the “Cash Collateral Investments”):

- Direct obligations of the United States Government.
- Other government securities, defined as securities issued, or guaranteed as to principal and interest, by the United States Government, its agencies or instrumentalities.
- Corporate debt securities, including repurchase agreements, commercial paper, bankers’ acceptances, medium term notes, floating rate notes, notes, debentures, and bonds; *provided, however*, that at the time of purchase, the securities described in this Paragraph must be rated as follows:
  - Long-term securities must be rated not less than A- by Standard & Poor’s Corporation or A3 by Moody’s Investor Services, Inc.
  - Short-term securities must be rated not less than A1 by Standard & Poor’s Corporation or P1 by Moody’s Investor Services, Inc.
- If a security is not rated by either Standard & Poor’s Corporation or Moody’s Investor Services, Inc., it shall not be purchased. Split-rated securities shall not be purchased. If any Cash Collateral Investment falls below the minimum rating standard, the Securities Lending Custodian shall make a recommendation to the Fund regarding its continued retention as a Cash Collateral Investment.

**Prohibited Investments.** Cash Collateral shall not be invested in any investment instrument not described above. For example, and not for purposes of limitation, the following investments are excluded:

- Common or preferred stock.
- Mutual Funds.
- Commodities.
- Derivatives of any kind regardless of their structure or guarantor, to include, but not be limited to, options, futures, mortgage-backed securities, asset-backed securities, range notes, swaps, interest-only securities, principal-only securities and inverse floaters. A floating rate note in which the interest rate is based upon a customary, recognized index shall not be deemed a “derivative” for the purposes hereof.
- Convertible debt.
- Foreign/international securities of any kind.
- Issues of affiliates or subsidiaries of foreign corporations, even if the affiliate or subsidiary is an American domiciled entity.
- Municipal securities.
- Unrated securities.
- Private placements.
- Issues of the Securities Lending Custodian, its parent, subsidiaries or joint ventures.
- Letters of credit by any issuer.

**Additional Requirements and Standards.** Any Securities Lending Custodian making Cash Collateral Investments shall also be bound by and subject to the following provisions:

- Any Cash Collateral Investment in the securities of any one issuer shall be limited to 5% of the total value, or amount, of the Cash Collateral, except that this restriction shall not apply to the investments in direct obligations of the United States government and other government securities as defined in the Permissible Investments paragraphs above. This restriction also shall not apply to the counter party in a repurchase agreement investment.
- Cash Collateral shall only be invested in United States dollar denominated investments.
- The maximum maturity of any single security in which the Cash Collateral is invested shall be 365 days. The Securities Lending Custodian shall not invest in any security which will cause the dollar-weighted average portfolio maturity of the Cash Collateral to be greater than 90 days.
- The Securities Lending Custodian is authorized to select brokers and dealers for the execution of trades in connection with the investment of Cash Collateral, which broker or dealer may be an affiliate of the Securities Lending Custodian,

provided that a competitive execution price is obtained at the time of execution of the trade.

- The Securities Lending Custodian is authorized to invest in direct obligations of the United States government and other government securities as defined in the Permissible Investments paragraphs above purchased from and/or sold by the Securities Lending Custodian, or any subsidiaries or affiliates of the Securities Lending Custodian.

## **F. Monitoring**

The custodian and/or securities lending sub-agent is responsible for reporting fully on all aspects of the Securities Lending Program, including its operation and returns.

The Securities Lending Custodian shall provide the Fund with reports no less frequently than once a month reflecting the loan transactions during the period and showing (i) the total fees paid by borrowers in loans of securities against Securities Collateral (the "Premiums"), and the percentage share of such Premiums credited to the Fund's account; and (ii) the total income earned on cash collateral investments (the "Yield"), the amount to be deducted there from as due from the Fund to the borrowers under the borrowing agreements (the "Rebate"), and the percentage share of the remaining earnings (Yield minus Rebate) credited to the Fund's account. All amounts credited to the Fund shall be shown on a manager-by-manager, fund-by-fund basis.

The Staff (on its own or through its consultant) shall conduct an annual review of the Securities Lending Program. At this time, the Staff will also survey its investment managers to ensure they have not encountered any problems with the Program.

## **XL. PROXY VOTING POLICY**

### **XLI. Introduction**

The Fund is a large public pension fund and will become a significant equity investor in the stocks of corporate America. The Board recognizes its responsibilities as a fiduciary of the Fund. The Board believes that a proxy policy is an important element of its overall asset management. As an initial position, the Board believes a delegation of authority to other fiduciaries of the Fund, the Investment Managers, will be the most suitable approach.

Each Investment Manager who is retained by the Fund to buy, sell or manage common stocks which are Fund assets will have the responsibility of voting the common stock in accordance with their internal proxy voting policy and these guidelines. To the extent that a third-party is used to assist in some aspect of the Investment Manager's proxy voting, the Investment Manager must inform the Fund of the third-party used and their exact responsibility. In completing this responsibility, each Investment Manager is expected to take these proxy voting guidelines into consideration.

### **A. Guidelines**

In exercising the proxy voting authority delegated to it by the Board, the Investment Manager is to vote the proxies for the exclusive benefit of Fund members and

beneficiaries, realizing all Fund assets are governed by the exclusive benefit rule of the Internal Revenue Code applicable to qualified plans.

In voting the proxies of common stocks, the Investment Manager must act with the care, skill, prudence, and diligence of a prudent expert who is similarly situated and knowledgeable in the matters under consideration, as required under IC 5-10.4. The Board intends that this embody the most rigorous application of this standard, that the Investment Manager act with an eye solely to the best interests of the plan participants. Leigh v. Engle, 727 F2d 113, (7<sup>th</sup> Cir.1984).

These two requirements mandate that the Investment Manager conduct an individual review and analysis of each proxy issue prior to voting. In all cases, the long-term economic best interests of members and beneficiaries should guide the voting decisions.

#### **B. Reporting Requirements**

The Staff intends to monitor the voting decisions of Investment Managers. To allow this to occur, each Investment Manager who votes shares of common stock will document such votes and report to the Staff no less frequently than annually.

The report shall include at a minimum the following:

- A description of the process the Investment Manager uses to ensure that reasonable steps have been taken to allow for the timely voting of all proxies on all stocks which are held as of the record date.
- The action taken on routine proxies.
- The action, and rationale for the action, taken on non-routine proxies.
- A description of actions in terms of any effects on members and beneficiaries of the Fund, the Indiana economy and any special Indiana issues.

#### **C. Revocation of Voting Authority**

The Board may revoke the authority of a Investment Manager to vote the shares of common stock held by presenting a written revocation of voting authority to the Investment Manager.

### **X. SECURITIES LITIGATION POLICY**

#### **A. Statement of Intent**

This securities litigation policy is established to provide a process for the monitoring of pending legal actions in which TRF is a potential member of a plaintiff's class or otherwise possesses an independent right to a securities law claim. As a fiduciary, TRF has a duty to monitor and evaluate such actions in which it may potentially be a member or participant. This policy contains TRF's process and guidelines for evaluating the appropriate level of participation in securities litigation claims. Such levels may include:

- Participating as passive class member in class actions brought by others, and filing claims when action is settled/resolved.
- Enhanced participation as class member in class actions brought and led by others, by considering objections or comments on settlements.
- Active participation in class action litigation, including serving as a “lead plaintiff” pursuant to the Private Securities Litigation Reform Act.
- Opting out of the class action and pursuing separate litigation on behalf of TRF.

## **B. Identifying and Evaluating Potential Claims**

Claims may generally be identified either by internal staff, custodian, investment managers, the class action bar, or outside claims consultants/analysts. Staff will determine the most expedient method to identify claims in which TRF has an interest. If TRF may qualify to recover, further review by staff (and the outside consultant if one is selected) will be undertaken to determine if TRF should remain a member of the class or undertake a more active level of participation. Whenever staff is aware that TRF has sustained a loss of \$5 million or more in any one investment, the staff will actively investigate and consider whether the Fund should pursue an individual action or other more active level of participation. Consideration will be given to the following factors:

- Size of TRF’s damages measured by standards applicable to securities litigation.
- Strength of claims, including evaluation of defenses.
- Special circumstances which render TRF’s claims different from (stronger or weaker) than claims of typical class members.
- Venue of litigation.
- Availability of resources to pay a significant recovery (e.g. financial condition of target company, availability of insurance, multiple defendants such as auditors, underwriters, etc.).
- Qualifications of other lead plaintiff candidates and their counsel, and likelihood TRF would be selected a lead plaintiff.
- Relations of claims to other corporate governance issues of special interest to TRF or its participants, and impact on other TRF holdings.
- Potential for non-monetary remedies of special importance to TRF which other class members/lead plaintiffs may not pursue.
- Costs to TRF of separate litigation/lead plaintiff status such as discovery, and staff/Board time and resources needed to monitor litigation more actively.
- Whether the active involvement of TRF will likely add value to the potential recovery or management of the case.

If, after reviewing these factors and any others considered relevant, staff determines that additional examination is warranted and that the potential exists for TRF to add significant value to the claim by actively participating, or opting out of the potential class of litigants and pursuing a claim independently, review of the potential claim will be referred to an evaluation counsel, in accordance with the process outlined below.

**C. Evaluation Counsel**

If further evaluation is determined to be warranted, an evaluation counsel may be retained to perform additional due diligence regarding the claim. TRF may retain evaluation counsel through the issuance of an RFQ on a case by case basis, or by issuing an RFP that selects any number of firms to be subsequently used in individual cases. Additional due diligence may include, without limitation; assessment of the complaint, SEC filings and company disclosures, contacts with other investors, consideration of non-litigation alternatives, and potential conflicts with other class members. The evaluation counsel will make a recommendation to the Executive Director, the Chief Investment Officer, and the General Counsel as to whether more active participation or opting out of a class action and pursuing a claim independently by TRF, would add significant value to any other options for recovery. Evaluation counsel may also be asked to evaluate settlements of class actions and recommend whether TRF should object to, comment or opt out of a particular settlement. Evaluation counsel will not be eligible to serve as litigation counsel for TRF on any matter they have evaluated for TRF.

**D. Staff Review and Consultation with Board**

Following a review of the potential claim by staff and receipt of the recommendation of the evaluation counsel, the Executive Director, Chief Investment Officer, and the General Counsel to pursue an active role, the General Counsel will consult with the Board to determine whether active involvement is warranted by TRF. The Board shall then determine whether TRF should (i) simply remain a member of the class, (ii) remain in class, but seek lead plaintiff status, independently or with other institutional investors, or (iii) opt out of the class and pursue an independent securities litigation action.

**E. Selection of Securities Litigation Counsel**

If the Board approves active involvement in a securities litigation claim, an RFP or RFQ will be issued pursuant to the Investment Procurement Policy to retain appropriate outside counsel to pursue such claims directly on behalf of TRF. The Board shall select counsel deemed best able to represent TRF's interests in pursuing such action.

In cases when TRF initiates litigation because it has determined it would be best to work with another institutional investor, staff may recommend, and the Board may conclude, that the most sensible and cost effective source of legal representation will be the TRF General Counsel's Office or the legal counsel representing such institutional investor that TRF wishes to support.

**F. Case Management**

The authority to settle, withdraw from or otherwise terminate a securities litigation matter initiated by TRF rests with the Board, but the Board may delegate such authority to the Executive Director and/or General Counsel.

The Board shall receive a quarterly report regarding the status of all securities litigation matters.

**G. Custodian Role and Authority**

- Maintain and communicate data necessary to identify TRF's securities holdings and transactions in order to determine if TRF is a class member, calculate amount of TRF's losses and prepare proofs of claim.
- Collect and distribute to appropriate parties (i.e., monitoring firm, evaluation counsel, litigation counsel) all notices regarding the commencement, class certification and settlement of class action lawsuits in which TRF has an interest as an actual or potential class member.
- Collect and deposit into appropriate accounts all investment proceeds of TRF's claims.
- Establish and implement a procedure to identify all securities class actions filed by others in which TRF is or may be a class member.
- Timely file proofs of claim on behalf of TRF in all class actions in which TRF may participate as class member.
- Provide monthly reports to Executive Director regarding status of all class actions in which TRF is a class member, including status of all proofs of claim.



## **XI. INVESTMENT MANAGER'S ACCEPTANCE**

We are in receipt of the Investment Policy Statement for the Indiana State Teachers' Retirement Fund dated August 1, 2006 and fully understand the terms and conditions contained therein. In particular, we understand our specific duties and responsibilities and understand the performance measurement standard to be applied to our management of the retirement assets.

We acknowledge and agree as to our fiduciary responsibility to fully comply with the entire Investment Policy Statement.

\_\_\_\_\_  
Date

\_\_\_\_\_  
Full Name of Investment Manager

\_\_\_\_\_  
Signature

\_\_\_\_\_  
Printed Name

\_\_\_\_\_  
Title

## APPENDIX I

First Asset Allocation (September, 1997):

<b><u>Asset Class</u></b>	<b><u>Target</u></b>	<b><u>Allowable Range</u></b>
Domestic Equity	36%	31% to 41%
International Equity	10%	8% to 12%
Fixed Income	48%	45% to 51%
REITS	6%	5% to 7%

Second Asset Allocation (November, 2001):

Domestic Equity	35%	30% to 40%
International Equity	15%	13% to 17%
Fixed Income	40%	37% to 43%
Private Equity	5%	4% to 6%
Real Estate	5%	4% to 6%

Third Asset Allocation (April, 2004):

Domestic Equity	42%	37% to 47%
International Equity	18%	16% to 20%
Domestic Fixed Income	25%	22% to 28%
Private Equity	5%	4% to 6%
Real Estate	5%	4% to 6%
Absolute Return	5%	4% to 6%

Fourth Asset Allocation (September, 2006):

Domestic Equity	35%	30% to 40%
International Equity	20%	16% to 24%
Fixed Income	20%	15% to 25%
Private Equity	10%	8% to 12%
Real Estate	7%	5% to 9%
Absolute Return	8%	6% to 10%

**ADDENDUM**

**TO**

**INDIANA STATE TEACHERS' RETIREMENT FUND**

**RESTATEMENT OF INVESTMENT POLICY**

**FOR**

**ANNUITY SAVINGS ACCOUNT**

Originally Adopted December 4, 1997 Last Restated August 1, 2006

## **I. INTRODUCTION**

### **A. Purpose**

This Addendum to the Indiana State Teachers' Retirement Fund Restatement of Investment Policy is intended to assist the Board of Trustees ("Board") of the Indiana State Teachers' Retirement Fund ("Fund") in managing the investment program established for the Annuity Savings Accounts.

### **B. Statutory Authority**

The Annuity Savings Accounts are bookkeeping accounts established for each member of the Fund. The member's account is credited with the member's 3% contribution (whether paid by the member or "picked-up" by the employer). The member has investment direction to several alternative funds or may leave their account in the "guaranteed fund." The guaranteed fund affords the member a capital preservation option on all contributions credited to that member's account, plus all previously credited interest (at an interest rate determined by the Board each year). These accounts produce an additional separate benefit from the fixed-formula employer-funded pension benefit. The Annuity Savings Accounts are subject to the following provisions:

- The Board must maintain a "guaranteed fund" option. IC 5-10.2-2-3(b).
- The Board must maintain an indexed stock fund option. IC 5-10.2-2-3(c)(I).
- The Board must maintain a bond fund. IC 5-10.2-2-3(c)(I).
- The Board may establish any other options it wishes, so long as the options represent a variety of investment objectives. IC 5-10.2-2-3(c)(2).
- With the exception of the guaranteed fund option, administrative costs of each of the options must be paid from the earnings on that option. IC 5-10.2-2-3(c)(4).
- A valuation of each member's Annuity Savings Account must be completed no later than the last day of each quarter. IC 5-10.2-2-3(c)(5).

### **C. Primary Focus**

The primary focus of this Addendum to Investment Policy Statement is to:

1. Outline the number and characteristics of investment options selected by the Board for the Annuity Savings Accounts.
2. Provide rate-of-return objectives and establish formal criteria to monitor and evaluate the performance results of the various investment options.

## **II. OBJECTIVES AND STRUCTURE OF THE ANNUITY SAVINGS ACCOUNT INVESTMENT PROGRAM**

This Policy has been structured to provide Plan members with a choice of five diverse options that offer a range of risk and return characteristics appropriate for members. A member can select between the options subject to the following conditions from IC 5-10.2-2-3(e):

- A member may make a selection or change an existing selection under rules established by the Board, but must be allowed to change at least once each quarter.
- The Board must implement the member's selection beginning the first day of the next calendar quarter that begins at least thirty (30) days after the selection is received by the Board. This date is the effective date of the member's selection.
- A member may select any combination of the Guaranteed Fund or any available alternative options, in ten percent (10%) increments.
- A member's selection remains in effect until a new selection is made.
- On the effective date of a member's selection, the Board must reallocate the member's existing balance or balances in accordance with the member's direction, based on the market value for an alternative investment option on the effective date and by account balance for any Guaranteed Fund balance on the effective date. The Board shall not reallocate the member's account at any other time.
- All further contributions to the member's account shall be allocated in accordance with the member's most recent effective direction.

The options currently include:

- Guaranteed Fund
- Bond Fund
- S&P 500 Index Fund
- Small Cap Equity Fund
- International Equity Fund

The number and types of investment funds available will be periodically reviewed by the Board in order to ensure a diversity of investment alternatives, adequate and reasonable availability of investment types, and clarity and usefulness of the investment choices. The objective will be to provide, on an ongoing basis, a broad array of investment choices representing diverse investment types described by the underlying capital markets, investment return expectations and risk expectations (defined as volatility of

investment return). The Board will also review the investment managers of the funds as provided for in Sections V of the Statement of Investment Policy.

Annually, the Board is required to prepare a separate analysis of the fund options for distribution of the participants describing recent and historical performance results in terms expected to be understandable to the average participant. This analysis must:

- Include a description of the procedure for selecting an alternative investment program;
- Be understandable by the majority of members; and
- Include a description of prior investment performance. IC 5-10.2-2-3(d).

### **III. INVESTMENT POLICY GUIDELINES**

#### **A. Guaranteed Fund**

The investment objective of the Guaranteed Fund is to provide stability with corresponding minimal risk, to have appropriate income yields, and to seek preservation of capital. The Board has selected a mix of 90% fixed income securities and 10% equity securities for this fund. The interest crediting rate earned by participants in the Guaranteed Fund fixed for the year and determined by the Board on an annual basis.

#### **B. Bond Fund**

The objective of the Bond Fund is to provide investment in the broad domestic bond market. In addition to investing in a broad range of investment-grade corporate, U.S. government and agency instruments this fund may invest up to 10% in high yield and 10% in non-U.S. fixed income securities.

#### **C. S&P 500 Index Fund**

The investment objective of the S&P 500 Index Fund is to provide investment in the broad domestic equity market. The S&P 500 Index Fund should closely track the returns of the S&P 500 Index by employing an indexing strategy that invests primarily in the stocks and futures of the S&P 500 Index.

#### **D. Small Cap Equity Fund**

The investment objective of the Small Cap Equity Fund is to provide investment in the stock of smaller domestic companies, typically referred to as small or medium cap stocks. The Fund will be invested with one or more domestic small cap and/or small to medium cap managers with the objective of producing returns in excess of the Russell 2000 Index.

#### **E. International Equity Fund**

The investment objective of the International Equity Fund is to provide a broad exposure to foreign equity markets of large companies based outside the United States. The Fund will be invested with one or more international equity managers with the objective of producing returns in excess of the MSCI EAFE Index.

#### **IV. PERFORMANCE OBJECTIVES**

The Board has determined that it is in the best interest of the Plan's participants and beneficiaries that performance objectives be established for each investment alternative and it is clearly understood that these objectives are to be viewed over the long term and have been established after full consideration of all factors set forth in this Addendum. The performance of each individual option will be evaluated relative to a market index and to a meaningful peer group of active managers. The evaluation of performance results will be accomplished according to the standards established in Section V of the Statement of Investment Policy. Specific benchmarks for each option are delineated below.

- Guaranteed Fund – The interest crediting rate will be determined by the Board each year based on the markets, the return of the Fund and other factors deemed relevant.
- Bond Fund - Lehman Brothers Aggregate Bond Index
- S&P 500 Index Fund - Standard & Poor's 500 Index
- Small Cap Equity Fund - Russell 2000 Index
- International Equity Fund - Morgan Stanley Capital International (MSCI) Europe Australia Far East Index.